

# Direct Negotiation and the Impact on Supplier Performance

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**Abstract**— The main objective of this study is to explore the public procurement on the Direct Negotiation issues. There are various types of public procurements implemented in the Malaysian government procurement system, however, Direct Negotiation has become the contractors' opportunities in abusing the system where many projects have failed to be completed as scheduled and others were completed with below standard which has not achieved the expectations. As stated in Ministry of Finance Circular 2013, the Direct Negotiation can only be awarded when there is urgent requirement, only for expert and credible contractor. This study has collected data from the Auditors General annual report from year 2015 until 2018, focuses mainly on auditor's observation on Direct Negotiation issues. Despite many comments from the public on the corrupt practice in the public procurement, this study has identified that there might be non-compliance on the decision in appointing the contractor for the Direct Negotiation which many issues arise in Auditor General report were on inefficiency of the contractor which has defeated the purposes on awarding the project through Direct Negotiation to credible contractor. Therefore, this research has agreed and supported that in order to be transparent and open, the Malaysian Government should eliminate Direct Negotiation and apply open tender on all public procurement.

**Keywords**— Public Procurement, Government of Malaysia, Auditor General, Open Tender, Direct Negotiation

## 1. Introduction

Transparency in the public procurement procedures has become the top priority [1]. The Malaysian Government has improved the procurement process especially the open competition in the tender. Close attention has been given in achieving goal of fairness, competition and best value for money.

However, it is a big challenge for the new government under the Pakatan Harapan to eliminate the Direct Negotiation which has been in the system for quite sometime. The government believes by abolishing the Direct Negotiation, it

will promote competition, less corruption, fraud and waste which will definitely minimise the mismanagement in public funds [2].

In discussing on the eliminating of Direct Negotiation, previous studies were done regarding the unethical conduct of public procurement [3], however, few studies have been carried out on the impact of direct negotiations towards the contractor's performance. Even though the government can impose action towards the contractor upon failing to adhere on the contract clause [4], it has been found that those contractors were getting away with the penalty and were awarded with another Direct Negotiation since contractor performance were only being analyse if its previous contract convicted with issues and been terminated or late delivery 30 percent later than expected accomplish date. Others have the record of renegotiation and restructure of the contract deliverables based on the contractor request [5], [6].

This paper discussed on low supplier performance that may cause by the key failings in Direct Negotiation Malaysia public procurement.

## 2. Literature Review

### 2.1. Public Procurement System in Malaysia

In the Malaysia Public Procurement System, there are three modes of procurement of goods and services namely; Direct Purchase, Quotations and Tenders. For Tenders, there are open tenders and non-tender; direct negotiation. The procurement method is stated as in Table 1.

**Table 1.** Procurement Method

Procurement Method	Procurement Value	Description
Direct Purchase	Up to RM 50,000	Item or any class of item amount up to RM 50,000 a year purchased directly from registered Bumiputera Supplier.
Quotation Procurement	RM50,000 to RM200,000	Quotation from at least 5 suppliers that registered with MOF for specific code of item.
Tender	Above RM200,000	Invited to all suppliers for all public procurement. Tender is not limited to open tender but also direct negotiation depending on need or specific expertise required.

This procurement methods to be followed by all the Malaysian government agencies and supported with other guidelines such as Treasury Instructions, and Treasury Circular.

As far as the government agencies concern, whatever methods choose and whoever being awarded, the contractor must understand their obligations and delivery according to both government and contractor agreeable terms [7].

## 2.2. Trends in Direct Negotiation

Direct negotiation is a purchase made directly from one single supplier. Direct negotiation is only applicable in fulfilling urgent requirement where price factor is not the main consideration only if the selected supplier is expert and has wide experience on the goods and services supplied [8], [9]. When agency choose to opt for direct negotiation, the procurement process will be exempted from open tender. Hence, this has eliminate the option of prequalification and selection of best performance contractor [10].

It was found that direct negotiation has become a trend where the open tender procurement were oft-abused. Some of these Direct Negotiations are much higher cost in which the contractor were taking advantage to maximise profit [11]. Several being awarded based on political influenced [3]. In 2018, the Auditor General report also stated that there was serious misgiving. Many of these government procurements were being direct negotiation without any strong justification.

By choosing direct negotiation, the government agencies are open to backdoor deal [12]. For instance, contract awarded through direct negotiation were given to political cronies. Much of this is related to procurement fraud and corruption. This was caused by information on the public procurement was not transparent and non-secrecy. Therefore, the tender information were not disclose [13] and only available to the political influenced contractors [12].

The objectives of public procurement is to support the government activities by acquiring goods and services with best value for money that benefit to the people. However, it is being misuse of power and being manipulated for the benefit of senior government officers and corrupt minister [12].

## 3. Methodology

This study investigated the trend and the issues related to Direct Negotiation in the Public Procurement in Malaysia. The author has reviewed the Auditor General Report published by National Auditor Department. Data was collected using content analysis from the Auditor General Report in 2015 until 2018. However, the author could not review the Auditor General Report for 2019 since the report has not been published during this study.

Direct negotiation issues reported in the Auditor General Report took place in the Ministry and Government agencies which happened were not only caused by the failure of the appointed contractor, it was also caused by inefficiency of the Ministry and Government agencies personnel who did not closely monitor the progress of the project. Therefore, the author has segregated the direct negotiation issues into two; issues related to failure of appointed contractor and inefficiency of ministry and government agencies. Since this study were studied only on the impact of supplier performance,

the result were only discussed on issues related to the failure of appointed contractor.

#### 4. Findings

There are many issues have been discovered related to Direct Negotiation. From the document review through Auditor General Report 2015 to 2018.

##### 4.1. Direct Negotiations Issues

Cases related to Direct Negotiation issues reported in Auditor General Report 2015 to 2018 as stated in Table 2. All the project issues took place when the project has been awarded to the contractor.

**Table 2.** Issues in Direct Negotiation Project

Project	Project Issues
Direct negotiations for Special Fisherman Housing Project under Fisheries Development Authority Malaysia	The programme was aimed to built new home for fishermen. The contractor failed to complete the project even though time extension were given to the contractor [14].
Direct negotiation for Desa Lestari Programme under Ministry of Rural and Regional Development	Desa Lestari Programme was launched to transform the rural areas in 80 selected villages into high-incomed resident. 19 projects from the programme were unsuccessful and abandoned [15].
Direct negotiation for eKadaster Project under Department of Survey and Mapping Malaysia	Implementation of eKadaster Project did not achieve the target. Inconsistency of the system requires for fund for system maintenance [15].
Direct negotiation for construction of Bera Hospital Pahang under Ministry of Health and Ministry of Public Works.	The construction of the hospital was not satisfactory where the appointed contractor failed to perform although the contractor has been given project extension for 23 months [15].
Project	Project Issues
Direct negotiation	The development of RC and

for Road Charges (RC) and Vehicle Entry Permit (VEP) under Ministry of Transportation.	VEP system was not completed even though the contractor has been given three times project extension of time [16].
Direct negotiations for Rural Water Supply Programme under Ministry of Rural Development	The water treatment project in Orang Asli areas in Pahang should have brought benefit to the Orang Asli population however the supply of clean water was unsuccessful where 15 out of 27 water treatment projects failed to operate [16].
Direct negotiations for reconstruction and upgrading school project under Ministry of Education	Deficiency of reconstruction and upgrading dilapidated schools project should be completed according to schedule. However, 328 schools out of 294 were not completed [16].
Direct negotiations for FELDA second generation settlers housing project	Development of housing project for FELDA second generation. Poor project monitoring which resulted poor construction quality and land erosion. Only 1,498 out of 20,000 houses completed
Direct negotiations for PERMATA Pintar Programme.	PERMATA Pintar Programme was aimed to provide educational needs to gifted and talented children. 10 contracts were not signed by authorised officers and acquisition of equipment was carried out without approval [17].

#### 5. Discussion

Based on the document analysis from the secondary data, it was found that implementation of Direct Negotiation for Public Procurement Tender was less than satisfactory due to inefficient of the contractor that has been appointed through closed deal during Direct Negotiation. According to the Ministry of Finance Circular, Direct Negotiation in Public Procurement was only allowed for urgent requirement and only one supplier or expert can provide specific goods or service. This procurement through Direct negotiation must be from credible supplier and approved by the Ministry of Finance. However, from the auditor

general report, it was found that almost all the auditor's observation shows that the issues were on late delivery of the project and inefficiency of the contractor. It shows that, the late delivery was caused by failure in identifying the right supplier. The result of the auditor was contradicting with the principle and terms allocated for direct negotiation.

## 6. Conclusion

Direct negotiation is a procurement process than can actually help the government to purchase goods and services in the fastest time provided the appointed contractor is expert and credible. From this study, issues discussed were related to unethical, misbehave and unsatisfactory of public procurement delivery proved that some Ministry and Government agencies has defeated the purposes of having Direct Negotiation in the public procurement. Therefore, it is the right time for the Government of Malaysia not to continue with the option of Direct Negotiation in the public procurement. Taking into consideration on many issues impacted on Direct Negotiation, starting from May 2018, the new government under the Pakatan Harapan has reviewed all direct negotiation projects and procurements. The government now does not grant any procurement under Direct Negotiation. This study has contributed the understanding on the issues and impact of Direct Negotiations and to support the Government of Malaysia on the decision to practise open tender procurement which is more transparent since direct negotiation has wasted so much of the government money.

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